



OPPORTUNITIES FOR STREAMLINING TAXATION OF THE TELECOMMUNICATION SECTOR IN EAST AFRICA





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UNDERSTANDING THE DIGITAL ECONOMY

1.0 Background

Digital transformation is one of the key drivers of the global economy. Digital economy refers to any economic activity that results from online connections among people, businesses, institutions, devices, data etc. It encompasses the broad range of economic activities that involve the utilization of Information and Communication Technologies (ICT) plus the internet which includes trade in electronic transmissions; online platforms or platform-enabled services; supply of ICT goods or services; mobile technology or applications including money transfer, borrowing, and saving services, among others. Digital economy also comprises digital platforms like Google, Facebook and Amazon, platform-enabled services such as car-hailing apps, plus ICT goods and services suppliers. Mobile technology and applications such as money transfer, lending or saving services also constitute the digital economy (Action Aid, 2020).¹ The digital economy thrives on the interconnectedness among people, organizations, and machines that are all enabled by mobile technology, the internet, and the Internet of Things (IoT). By reducing transaction costs, thus improving market efficiency, telecommunication enables economic development (Aker and Mbiti, 2010).²

East African countries have been characterized as ‘Break Out’ economies, according to the Digital Intelligence Index Report by MasterCard and the Fletcher School at Tufts University.³ This characterization is attributable to the rapid growth in internet penetration and substantive improvements in digital infrastructure in the region’s member states. Consequently, the improved digital economy landscape has resulted in a better environment for owners of small businesses to thrive.

Key to the robust and growing digital economy in the region is the telecommunication sector. In Africa, the mobile ecosystem is valued at about USD115 billion and contributes 9% of the continent’s GDP.⁴ Africa’s digital economy is projected to reach a value of about USD712 billion by 2050 while contributing USD200 billion to the continent’s GDP as of 2023 compared to an economic value of USD132 Billion in 2020 with tax contributions of USD15 billion. The sector is significant to East Africa’s economy. It is estimated that a percentage point increase in the telecom index usage (fixed line, mobile cellular and internet) contributes to a 0.02 real per capita growth.⁵ With increased investment and technological adoption of advanced technologies, the telecom sector demonstrates significant potential for growth with the likelihood of becoming a crucial and pronounced pillar to the region’s economy.

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1. Action Aid, *Taxing the Digital Economy*, Progressive Taxation Policy Brief, January 2020 <https://actionaid.org/sites/default/files/publications/Digital%20taxes%20progressive%20tax%20brief%20jan20.pdf>
 2. Aker J.C., and Mbiti I.M., ‘Mobile Phones and Economic Development in Africa’, *Journal Of economic Perspectives*, Vol. 24, No. 3, Summer 2010, (pp. 207-32), <https://www.aeaweb.org/articles?id=10.1257/jep.24.3.207>
 3. Kitimo A., ‘Kenya, Tanzania and Rwanda rank top for rapid digital growth, demand’, *The East African*, 16 December 2020, <https://www.theeastafrican.co.ke/tea/news/east-africa/kenya-tanzania-rwanda-rank-top-for-rapid-digital-growth-3230890>
 4. Herbert G. and Loudon L., *The size and growth potential of the digital economy in ODA-eligible countries*, K4D (Knowledge, Evidence, and Learning for Development) Helpdesk Report, 1 December 2020, https://opendocs.ids.ac.uk/opendocs/bitstream/handle/20.500.12413/15963/915_size_and_growth_potential_of_the_digital_economy_in_ODA-eligible_countries.pdf?sequence=1&isAllowed=y
 5. Kedir A., Kawo K.N., and Hasan A., ‘ICT and Economic Growth in East African Countries: A Panel Data Approach’, *Journal of Information Engineering and Applications*, Vol.9, No.7, December 2019, (PDF) [ICT and Economic Growth in East African Countries: A Panel Data Approach](#)

1.1 Rationale for the Study

As with the rest of the world, East African countries acknowledged the fundamental significance of the digital economy in accelerating economic growth. Considering this fact, especially in reference to the telecom sector's value to the region's economy, there is a need for the regional governments to adopt and implement robust policies to govern the sector. More specifically, the governments should consider enforcing a progressive tax regime on the sector to maximize its potential contribution to the economy. However, research currently shows the inefficiencies of the existing taxation models and overall challenges in taxing the telecom sector. There are gaps in policies and regulations, which, it has been argued, provide loopholes for opaqueness in reporting revenue figures by industry players, therefore, allegedly resulting in tax evasion by telecommunication industries. On the government side, there is arguably limited expert knowledge in taxing the telecom sector. There is also weak enforcement of the existing tax regime to ensure full compliance by all players in the sector.

As such, the purpose of this study is to examine the landscape of the digital economy with a narrow focus on the telecoms sector. The study sought to examine the taxation regime in the sector by focusing on gaps in policies and regulations in the sector, the challenges, and opportunities for taxing the telecom sector and the digital economy. The specific objectives of the study were:

1. To examine challenges associated with mobilizing revenues from the telecom sector and the digital economy.
2. To determine opportunities to be leveraged to improve tax revenue mobilization from the telecom sector and digital economy.

2.0 Introduction

The telecom sector in East Africa is transforming and growing rapidly. The contribution of the sector to the individual economies of the region has also expanded substantively over the last two decades.

However, there still remains substantive gaps that limit its contribution to the region's economy. This brief explores opportunities emerging from these gaps and challenges in order to identify ways to help improve the operating environment of the telecom sector, streamline tax policies, and enhance the contribution of the telecom sector, and the digital economy in general, to the revenue base for financing development priorities in the region.

2.1 Opportunities for Tax Rationalization for Telecoms in East Africa

- a) **Operationalize a single digital market and regulatory body in East Africa:** After developing a road map for the Single Digital Market (SDM) in 2018, the implementation of this strategy is yet to happen. The presence of an SDM in East Africa would ensure a competitive regional digital ecosystem that could drive a reinforcing cycle of economic growth, investment, innovation, job creation and improved service delivery. Successful implementation of the SDM, with a single regulatory body, would also ensure a harmonization of laws and policies that would boost the growth of the single digital market.
- b) **Standardize tax policies:** The current tax landscape in the region exhibits significant disparities among member states. This inconsistency creates unpredictability for investments in the telecom sector and the larger digital landscape. Harmonizing tax policies presents an opportunity to streamline and standardize taxation across the region.
- c) **Simplifying the tax system:** Telecom industry experts and taxation professionals have highlighted the complexity of the tax system for telecom companies. This complexity poses challenges for both telecom operators in meeting their tax obligations and regulatory authorities in monitoring compliance. Simplifying the tax system would enhance accountability and oversight in the sector by making these processes clearer.
- d) **Adoption of ICT:** It has been noted that tax authorities across East Africa tend to be slow in adopting advanced systems powered by latest technology which limits their ability to effectively monitor the operations of the telecom sector operators. It also creates a gap that can be exploited by the telecom operators to hide their operations and evade tax. Considering the rapid pace of evolution in the telecom sector, it is critical that tax and regulatory authorities adopt advanced systems powered by the newest technologies if they are to effectively play their oversight role.
- e) **Focus on capacity development:** There is a demonstrated need for capacity development for regulatory authorities and other actors in the telecom sector. The skills necessary for monitoring industry operations and enforcing tax obligations as mandated by the law need substantive investment in continuous capacity enhancement – both human and technological. For regulatory authorities, experts knowledgeable in taxation of the telecom sector are required to streamline the tax regime and ensure that opportunities for tax evasion are identified and addressed.
- f) **Prioritize data protection:** Data privacy and security is a significant challenge in monitoring the operations of the telecom sector. As such, there is a need to institute a robust legal framework that would guarantee data protection while providing sufficient room for regulatory authorities to monitor all activities and operations of the telecom sector.

- g) Strengthen laws and policies to enable telecom companies to improve transparency in reporting:** There is a need to create and enhance laws and policies that specifically require telecommunication companies and other digital economy players to provide complete information disclosure about their income-generating activities. Strengthening these laws and policies promotes transparency, reduces customer exploitation, and reinforces compliance. This policy should address the harmonization of ICT laws in the East African Community (EAC).
- h) Invest in training and development of revenue authority staff:** Training and developing the expertise of revenue authority staff is essential for the adoption of effective tax administration methods, including innovation and digitization. The training should be informed by a rigorous capacity assessment and include areas such as policy analysis, formulation, and include, all of which should be specifically tailored for the telecom sector.
- i) Implement a joint taxation strategy for the digital economy:** The EAC's current tax framework relating to the digital economy is fragmented and hinders economic integration. Developing a coordinated approach to taxing the digital economy of EAC's member states would significantly enhance tax predictability and fairness for businesses and encourage their participation in the regional market. This approach should address gaps in the legal frameworks and potentially improve the identification and taxation of digital economy players.
- j) Frequent and elaborate audits:** Frequent audits of telecom companies are essential to obtain accurate information about their operations and economic activities. Regular audits promote confidence in financial reporting and better communication among companies. However, governments in East Africa have demonstrated limited independent auditing of telecom companies, often relying on private auditing firms. This lack of rigorous auditing creates potential loopholes for false reporting and revenue leakages.

2.2 Recommendations

Regardless of the constraints faced in tax administration, there exist opportunities to enact effective reforms for streamlining tax collection and enforcing compliance. Below are some recommendations that players in the sector in the region (at country level or EAC) can pursue to promote effective enforcement of tax compliance⁶ and domestic revenue generation from the telecom sector in East Africa:

1. Revenue authorities at the national level to streamline revenue reporting requirements to ensure telecom companies regularly report itemized revenues for the different products offered to clients. Further, revenue should be reported based on the earliest consumption of service, issuance of invoice or receipt of payment.
2. Revenue authorities at the national level to develop and harmonize standardized formats for data collection and reporting (use of a pre-formulated template) to simplify existing systems and ensure exhaustive reporting and easy monitoring of sector operators and revenue streams.
3. Revenue authorities, regulatory agencies, and telecom companies to invest in relevant capacity development and hire experts with necessary skills to ensure fulfillment of tax obligations and compliance with existing tax requirements for the sector.
4. Revenue authorities and regulatory agencies to improve communication with telecom operators on undertakings such as ongoing network upgrades and invest more resources and efforts in monitoring capital expenses, and repairs and equipment maintenance costs incurred by operators.

6. Akitoby B., 'Raising Revenue', *Finance and Development*, IMF (International Monetary Fund), December 2018, <https://www.imf.org/external/pubs/ft/fandd/2018/03/akitoby.htm>

5. EAC secretariat and member states to pursue and operationalize a regional governance framework to oversee telecom operation in the region and streamline tax policies in the industry.
6. National tax authorities to invest in, adopt and apply ICTs in tax administration for the region to benefit from technology-driven tax systems that promote effective administration and confirmatory compliance.
7. Authorities at the national level to harmonize policy and institutional frameworks to ensure that relevant agencies overseeing the sector have clear mandates to reduce duplication of regulation that compound administrative costs for operators.
8. CSOs to broker stakeholder engagements to achieve political commitment and buy-in from all key stakeholders to guarantee tax policies and other industry regulations are streamlined, and to guarantee telecom sector operations comply fully with taxation requirements as mandated by the existing compendium of laws.



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